

ICAP SEF Market Regulation Advisory Notice

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| From | <i>ICAP SEF (US) LLC ("ICAP SEF")</i> |
| To | <i>All ICAP SEF Market Participants</i> |
| Subject | <i>Revised Rulebook – STP for Cleared Swaps</i> |
| Rule References | <i>204(i), 502, 516</i> |
| Notice Date | <i>11 July 2016</i> |
| Notice Number | <i>ICAP-2016-4</i> |

On Monday, July 11, 2016, ICAP SEF filed amendments to the ICAP SEF Rulebook with the Commodity Futures Trading Commission ("CFTC") in response to the CFTC's Division of Market Oversight letter from December 21, 2015 concerning requirements for the straight-through processing ("STP") of intended-to-be-cleared ("ITBC") swaps executed on SEFs. These amendments are scheduled to take effect on August 1, 2016.

On December 21, 2015 the Commission published Letter 15-67, which provides supplemental guidance on the straight-through processing of swaps, including the requirement that the SEF develop rules and procedures so a Cleared Contract may be accepted or rejected for clearing as quickly after execution as would be technologically practicable if fully automated systems were used ("AQATP"). In order to meet the AQATP standard, Letter 15-67 mandates that a Cleared Contract must be routed to and received by the relevant DCO no more than 10 minutes after execution on the SEF, although a longer period is permissible in the event errors in the Cleared Contract are discovered and corrected. The letter also notes that Cleared Contracts may be routed directly to a DCO or through an Affirmation Hub. In preparation for the August 1, 2016 compliance date set forth in Letter 15-67, the SEF has amended its Rulebook to set forth new Rules designed to meet the 10 minute AQATP standard to explain the new Rules to Participants, each as discussed below.

- Rule 204(i) has been added to the Rulebook to require the SEF to route Cleared Contracts to the relevant DCO no later than 10 minutes after execution, either directly to the DCO or through an Affirmation Hub. Where an Affirmation Hub is used, Rule 204(i) requires Participants and Customers to Affirm, within the 10 minute AQATP standard required by Letter 15-67, any Cleared Contract executed as a Pre-Arranged Cross (other than those resulting from Bids/Offers generated by a Bulk Risk Mitigation Service) or with the assistance of an Execution Specialist. All other Cleared Contracts (including those resulting from Bids/Offers generated by a Bulk Risk Mitigation Service) will be marked by the SEF for "autoprocessing," which means the Cleared Contract will be automatically submitted to the DCO by the Affirmation Hub without providing Participants or Customers the opportunity to Affirm the Cleared Contract. Because the SEF's procedures are designed to send a Cleared Contract to the Affirmation Hub immediately after execution, Rule 204(i) is designed to ensure the 10 minute AQATP standard is met for each Cleared Contract, regardless of whether a Participant must Affirm a Cleared Contract or the Cleared Contract is marked for autoprocessing. Failure by a Participant or Customer to meet the 10 minute AQATP standard will be a Violation, unless the SEF determines the failure was due to errors or delays caused by the SEF or an Execution Specialist. Violations of Rule 204(i) may be subject to the formal disciplinary procedures set forth in Chapter 5 of the Rulebook, or to new Rule 516, which provides for summary fines as discussed below. The Definitions have been amended to add definitions of "Affirm," "Affirmation Hub" and "Bulk Risk Mitigation Service," which are used in Rule 204(i).
- Investigations of alleged Violations of Rule 204(i) will be conducted in accordance with existing Rule 502. However, new Rule 516 has been added to provide the Chief Compliance Officer with the authority to impose summary fines on Participants and Customers that have failed to Affirm a Cleared Contract within the 10 minute AQATP standard required by Rule 204(i). Any Participant that is an Intermediary may be held responsible for a Violation of Rule 204(i) by its Customer. Rule 516 sets forth procedures for notifying a Participant or Customer that a summary fine will be imposed and permits the Participant or Customer to contest the summary fine, in which case the alleged Violation

shall be subject to the formal disciplinary procedures set forth in the existing provisions of Chapter 5, and not governed by Rule 516. The authority to impose summary fines does not prevent the Chief Compliance Officer from instead submitting a Violation of Rule 204(i) to the Review Panel in accordance with the existing formal disciplinary provisions of Chapter 5. Additionally, in the event a Participant or Customer has received aggregate summary fines up to the maximum amount permitted by Rule 516, the Chief Compliance Officer may then submit any additional Violations of Rule 204(i) to the Review Panel in accordance with the existing formal disciplinary provisions of Chapter 5, which may result in additional sanctions beyond the summary fines. The imposition of summary fines pursuant to Rule 516 is designed to increase compliance with Rule 204(i), and thereby increase the SEF's ability to ensure the 10 minute AQATP standard is met. Rule 502(c) has been amended to reference the new summary fine procedures set forth in Rule 516.

FAQ Related to 10 Minute STP Requirement and ICAP SEF Rule 204(i) and 516

1. What is the 10 minute STP mandate?

The CFTC's Division of Market Oversight has issued further guidance¹ on straight-through processing for ITBC swaps executed on SEFs. This latest guidance mandates that on August 1, 2016, all ITBC swap transactions executed on a SEF must be routed to and received by the Derivatives Clearing Organization ("DCO") within 10 minutes after execution. In preparation for the August 1, 2016 compliance date and after discussing the issues and solutions with customers, ICAP SEF has developed policies and implementation schedules to meet the requirements in the CFTC's guidance. ICAP SEF's policy reflects the market's current readiness for straight-through processing and operational concerns for the different execution methods offered by ICAP SEF.

2. What is the product scope covered by this rule?

All ITBC swap transactions executed on a SEF are covered under the CFTC guidance, ICAP SEF Rule 204(i), and ICAP SEF Rule 516. This will include both voluntarily cleared and mandatorily cleared swap transactions.

3. Is this a "new" requirement?

As discussed in the CFTC's Letter No. 15-67, the Commission's regulations require prompt clearing through Regulation 37.12(b)(7), 37.702(b), and 39.12(b)(7). Moreover, the Commission issued a 2013 Staff Guidance Letter² identifying that third-party hubs are permissible if the swap is routed "as quickly after execution as would be technologically practicable if fully automated systems were used." While the most recent guidance has provided a 10 minute measure to this requirement, the requirement to affirm transactions promptly has been in effect since 2013.

4. Will I still be able to affirm all cleared transactions?

All ITBC transactions generated by a Bulk Risk Mitigation Service (e.g., RESET) will be auto-processed. Non-ITBC transactions will continue to follow the existing workflows. All other applicable ITBC transactions executed on ICAP SEF will continue to be sent to a third party middleware provider (e.g., MarkitWire) for affirmation.

¹ <http://www.cftc.gov/idc/groups/public/@lrlattergeneral/documents/letter/15-67.pdf>

² <http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/stpguidance.pdf>

5. What happens if a trade is affirmed after 10 minutes?

If ICAP SEF determines based on the facts and circumstances that a customer had a reasonable opportunity to affirm the details and release the trade in the middleware systems within 10 minutes yet did not do so, the SEF participant would be in violation of ICAP SEF Rule 204(i)(3) and subject to sanctions as described in Chapter 5 of the Rulebook (see Question 11 for information about ICAP SEF's Summary Fine Schedule).

6. How does the SEF determine if a trade is affirmed after 10 minutes?

This is determined by measuring the time between the execution time of the swap transaction and when a transaction is sent to clearing by the affirmation platform (e.g., MarkitWire).

7. When are trades sent to middleware providers?

ICAP SEF delivers swap transactions to Participants immediately after the execution of a transaction.

8. Does the transaction stand if affirmed after 10 minutes?

Swap transactions that are not sent to clearing within the 10 minute will continue to be binding, enforceable transactions.

9. What if the trade has an error that requires correction?

As discussed in footnote 7 of the CFTC's Guidance Letter No. 15-67, it is understood that if an error is detected within the period, it may take longer than 10 minutes to complete the correction of the error and, thus, there would be no failure of the straight-through processing requirements. Moreover, ICAP SEF Rule 204(i)(3)(ii) clarifies that there is no Violation where the failure was substantially the result of, as determined in ICAP SEF discretion, any errors or delays caused by ICAP SEF or any Execution Specialist. While an error may provide a Participant more than the 10 minutes to resolve and properly process the transaction, this does not excuse Participants from taking all reasonable measures to affirm the transaction after the error has been properly resolved.

10. Can ICAP SEF determine which party is at fault if a trade gets held up in a middleware affirmation process?

Yes. ICAP SEF has visibility into the audit trail of post execution trade processing and will use this information when reviewing the activity for potential violations of Rule 204(i).

11. Is there a Summary Fine Schedule for violations of Rule 204(i)?

Yes. As described in Rule 516(e), ICAP SEF shall set the amount of any fine imposed pursuant to Rule 516, with a maximum aggregate fine for Violations of the same Rule, or subsection thereof, not to exceed \$7,000 on an annual basis. The following schedule lists the actions that the Compliance Function may take:

| Rule Violation | Action Taken Per each Violation in a Rolling 12-month period | | | |
|----------------|--|------------------|-----------------|--|
| | First Violation | Second Violation | Third Violation | Fourth Violation |
| Rule 204(i) | Warning Letter | \$2,000 | \$5,000 | Referral to Review Panel for formal disciplinary procedures. |

12. Is each instance considered a violation in terms of the Summary Fine Schedule?

As discussed in Rule 516(c), ICAP SEF may aggregate individual Violations and treat such Violations as a single offense.

13. Who is responsible for Violations of ICAP SEF Rule 204(i)?

As discussed in ICAP SEF Rule 516(a), summary fines may be imposed on Participants and Customers involved in the transaction. A Participant that is an Intermediary may be held responsible for a Violation by its Customer.

14. Can amendments be made to transactions after they have been cleared? How will these transactions be processed?

Yes. Please see ICAP SEF Rule 315 *SEF Authority over Transactions* for additional information under which the SEF will review and process amendments in the event an error occurs. In the case where a new transaction is executed due to an operational error, ICAP SEF has the functionality to process the new transaction with or without affirmation.

Contact

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